



## WISCONSIN ASSOCIATION OF HEALTH UNDERWRITERS

*Wisconsin's Benefit Specialists*

### **Assembly Committee on Insurance**

#### **Assembly Bill 107**

**April 18, 2007**

The Wisconsin Association of Health Underwriters (WAHU), along with agent associations, has developed the Sensible Health Care Solutions – a comprehensive health care reform plan. WAHU, and the Coalitions reform plan, are supportive of providing health insurance premium tax deductibility to Wisconsin consumers. Therefore, we generally support Assembly Bill 107. We believe that AB107 helps consumers afford health insurance coverage. The following is our position on tax deductibility of health insurance premiums:

#### **Sensible Health Care Solutions**

##### **7. Insurance/Market Reforms**

##### **Health Insurance Premium Tax Deductibility**

For the most part, the private market has done a good job of ensuring that the portion of the premium paid by employees is tax deductible to the employee. Roughly 50% of all employers have implemented a Section 125 plan. This section of the IRS Code allows employees to use before tax dollars to purchase certain health care related items, including premiums. The State too has done a good job in trying to make premiums deductible for those who are not covered by a group plan. In Act 25 (the 2005-07 Budget), state increased from 50% to 100% the amount of health insurance premiums that are deductible for employees whose employer doesn't pay anything toward health insurance. It also created a deduction (phased-in over time, to 100% in 2009) for people who aren't employed and don't have self-employment income. The Governor included a provision in his budget that would make health insurance premiums for all employees covered under their group plan tax deductible. In addition, AB107 would essentially do the same thing. While we support the Governor's budget provision and this legislative proposal that attempt to make these premium contributions tax deductible, we believe expanding Section 125 plans would be more valuable to Wisconsin consumers, as through a Section 125 plan, both state and federal taxes are deductible. These current proposals would only allow state taxes to be deductible. While we support these proposals, we believe the State should also provide private sector employers with tax incentives to implement Section 125 plans.





# State of Wisconsin • DEPARTMENT OF REVENUE

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**Jim Doyle**  
Governor

**Roger M. Ervin**  
Secretary of Revenue

## Assembly Committee on Insurance Hearing, April 18, 2007

### **Assembly Substitute Amendment 1 to Assembly Bill 107 (LRBs0024/1) – Creating an Individual Income Tax Deduction for Certain Medical Care Insurance Policy Premiums. (Representative Hahn)**

#### *Description of Current Law and Proposed Change*

The bill, as amended by ASA 1, allows a subtraction from income for the amount paid by a claimant for medical care insurance premiums for a policy that covers the claimant, the claimant's spouse, and the claimant's dependents. To be eligible for the deduction, the claimant must be the employee of another person and the claimant's employer must pay part, but not all, of the cost of the claimant's medical care insurance.

A similar provision is included in the Governor's 2007 budget bill. In the budget bill, the health insurance subtraction is phased in beginning in tax year 2008. Claimants will be allowed to deduct 10% of their share of medical insurance premiums in 2008, 25% in 2009, 45% in 2010, and 100% in 2011.

#### *Fairness/Tax Equity*

- Current law allows for 100% of health insurance premiums paid by the self-employed to be subtracted from income when calculating Wisconsin individual income tax. Similarly, a deduction is allowed for the premiums paid by employees whose employers do not contribute to health insurance coverage. In 2007 and 2008 a subtraction for health insurance premiums will be phased in for individuals with no self-employment income and no employer. In 2009 the full amount of premiums paid by those individuals will be deductible.
- This bill, as amended by ASA 1, allows the medical insurance premium deduction to the remaining individuals who are not included in existing laws. That is, it allows a deduction for employees whose employer contributes to the cost of health insurance, but requires the employees to pay for a portion of the premiums.

#### *Administrative Impact/Fiscal Effect*

- Based on a comprehensive medical care insurance premium deduction in Iowa, it is estimated that the employee share of medical care insurance that will be claimed is \$1.8 billion in tax year 2007. The original bill allows for a nonrefundable credit equal to the employee share of medical care insurance and it is estimated that \$1.0 billion to \$1.3 billion of the claimed credit could be used. The bill, as amended by ASA 1, allows a deduction rather than a credit for the employee share of medical care insurance. The tax year 2007

deduction is estimated to reduce revenue by \$109 million in fiscal year 2008 and the tax year 2008 deduction is estimated to reduce revenue by \$118 million in fiscal year 2009.

- Some taxpayers may adjust their withholding to take into account the anticipated decrease in their tax liability that this deduction will cause. The extent to which taxpayers will do this is unknown, but if all taxpayers do so, the fiscal year 2008 revenue loss could be as high as \$163 million. This estimate includes \$109 million associated with decreased tax year 2007 liability paid in fiscal year 2008 and \$54 million associated decreased withholding in fiscal year 2008 for tax year 2008.
- The language of the bill, as amended by ASA 1, provides that it applies for taxable years beginning after December 31, 2006. This would be a problem only if enacted late in the year after 2007 forms had been finalized. If enacted after July 31, 2007, it would be preferable if the language would provide that it apply for taxable years beginning after December 31, 2007.

#### *DOR Position*

- The Department of Revenue supports the proposal provided that the subtraction is phased in as specified in the Governor's 2007 budget bill.

Prepared by: Brad Caruth (608) 261-8984

April 16, 2007

BC:skr

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April 16, 2007

Representative Frank Lasee  
Room 105 West  
State Capitol  
P.O. Box 8952  
Madison, WI 53708

RE: AB 107 - Assembly Insurance Committee Hearing on April 18, 2007

Dear Representative Lasee:

On behalf of the **National Association of Insurance and Financial Advisors of Wisconsin** (NAIFA - Wisconsin), the **Independent Insurance Agents of Wisconsin** (IIA) and the **Professional Insurance Agents of Wisconsin** (PIA), we would like to express our **support for Assembly Bill 107**, creating a nonrefundable individual income tax credit for certain medical insurance policy premiums.

Neither of us can attend the Committee on Insurance hearing on April 18, 2007, so we submit this letter of support in advance of the hearing.

Sincerely,

**DEWITT ROSS & STEVENS** s.c.

Jordan K. Lamb

JKL:jkl

Ron Kuehn





## Legislative Fiscal Bureau

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April 17, 2007

TO: Representative Eugene Hahn  
Room 15 West, State Capitol

FROM: Faith Russell, Fiscal Analyst

SUBJECT: Individual Income Tax: Assembly Substitute Amendment 1 to 2007 Assembly Bill 107

At your request, I am providing an estimate of the fiscal effect of Assembly Substitute Amendment 1 to Assembly Bill 107, which would provide an individual income tax deduction for health insurance premiums paid by employees who pay part of such premiums. The deduction would apply for taxable years beginning after December 31, 2006. This memorandum starts with a description of current law, followed by a description of the substitute amendment and its estimated fiscal effect.

### **Current Income Tax Provisions Related To Health Insurance Premiums**

There are a number of provisions under current law that provide income tax exclusions and deductions related to health insurance premiums. Under current federal law, to which Wisconsin conforms, employers may offer fringe benefits in the form of cafeteria plans, which allow employees to choose between receiving cash (or other taxable benefits) or certain qualified benefits (including health benefits) for which the law provides an exclusion from wages for income tax purposes. Therefore, under a cafeteria plan, employees may select to have their share of employment-based medical care insurance paid with pre-tax dollars, thereby reducing the employee's taxable wages by the amount paid for the medical care insurance.

Current state law also provides deductions for 100% of long-term care insurance premiums and for medical care insurance paid for by self-employed individuals that do not exceed net earnings from a trade or business that is taxable by this state. Wisconsin also provides a deduction related to premiums paid by an employee whose employer did not contribute anything toward the cost of the medical care insurance. In such cases, prior to tax year 2006, Wisconsin law permitted a deduction of 50% of the premiums paid by the employee. Effective with tax year 2006, as provided under 2005 Act 25, an employee whose employer did not contribute anything toward the cost of the

medical care insurance may deduct 100% of the premiums paid by the employee. For purposes of these deductions, "medical care insurance" means a medical care insurance policy that covers a taxpayer, the taxpayer's spouse, and the taxpayer's dependents and provides surgical, medical, hospital, major medical, or other health service coverage.

In addition to the deductions described above, Act 25 created a deduction for medical care insurance premiums paid by an individual with no employer and no self-employment income, to be phased in over a three-year period beginning in tax year 2007 as follows: (a) 33.4% of the cost of such premiums are deductible in tax year 2007; (b) 66.7% will be deductible in tax year 2008; and (c) 100% of such premiums will be deductible in tax years 2009 and thereafter.

For non- and part-year residents, the current law deductions for medical care insurance premiums of employees and unemployed individuals must be pro-rated based on the share of total income that is taxable to Wisconsin. For self-employed individuals who are non- or part-year residents, the medical insurance premium deduction must be pro-rated based on the individual's share of income earned from a trade or business taxable to Wisconsin.

Finally, certain medical care insurance premiums are also eligible to be included in the calculation of the state's itemized deduction credit. The itemized deduction credit is equal to 5% of the excess of allowable itemized deductions over the sliding scale standard deduction. Medical expenses that conform to those permitted as federal itemized deductions, which include medical expenses exceeding 7.5% of federal adjusted gross income (AGI), are generally allowable for calculating the state itemized deduction credit. However, medical care insurance premiums that are subtracted from Wisconsin income (under one of the income tax deductions described above) are disallowed for purposes of the state's itemized deduction credit.

#### **Assembly Substitute Amendment 1 to Assembly Bill 107**

Assembly Substitute Amendment 1 to Assembly Bill 107 would provide an individual income tax deduction for 100% of medical care insurance premiums paid by an employee whose employer pays for some portion of the employee's health insurance costs, starting with tax year 2007. The proposed deduction would use the same definitions and general parameters as those in effect for the current law deductions. As with the current law deductions for employees and unemployed individuals, a non- or part-year resident would have to pro-rate the proposed deduction for medical care insurance premiums based on the individual's share of total income that is taxable to Wisconsin.

The proposal would specifically benefit employees whose payments for medical care insurance are not made with pre-tax dollars (which would be the case when the payments are not being made under a cafeteria plan).

### **Estimated Fiscal Effect**

The estimated fiscal effect of the proposal is based on information provided by the State of Iowa regarding the estimated cost of Iowa's general exemption for medical care insurance premiums. Based on the data from Iowa, after adjusting for differences in the number of taxpayers in the two states and current Wisconsin exemptions for medical care insurance premiums, it is estimated that the proposal would reduce state tax revenues from the individual income tax by \$109 million in 2007-08 and by \$118 million in 2008-09, for a total of \$227 million in the 2007-09 biennium.

Please let me know if you have additional questions.

FR/sas

1. The first part of the document is a letter from the President of the United States to the Congress, dated January 3, 1862. It is a very important document, as it contains the President's annual message to Congress. The letter is written in a formal, dignified style, and it is one of the most important documents in the history of the United States.

### THE PRESIDENT'S MESSAGE TO CONGRESS

2. The second part of the document is a report from the Secretary of the Interior, dated January 10, 1862. It is a very important document, as it contains the Secretary's annual report to the President. The report is written in a formal, dignified style, and it is one of the most important documents in the history of the United States.

### THE SECRETARY'S REPORT TO THE PRESIDENT

3. The third part of the document is a report from the Secretary of the Treasury, dated January 15, 1862. It is a very important document, as it contains the Secretary's annual report to the President. The report is written in a formal, dignified style, and it is one of the most important documents in the history of the United States.

### THE SECRETARY'S REPORT TO THE PRESIDENT

4. The fourth part of the document is a report from the Secretary of the War, dated January 20, 1862. It is a very important document, as it contains the Secretary's annual report to the President. The report is written in a formal, dignified style, and it is one of the most important documents in the history of the United States.

### THE SECRETARY'S REPORT TO THE PRESIDENT

5. The fifth part of the document is a report from the Secretary of the Navy, dated January 25, 1862. It is a very important document, as it contains the Secretary's annual report to the President. The report is written in a formal, dignified style, and it is one of the most important documents in the history of the United States.